FCC 92-207

IN THE MATTER OF

BUNDLING OF CELLULAR CUSTOMER PREMISES EQUIPMENT AND CELLULAR SERVICE
CC Docket No. 91-34
Adopted: May 14, 1992; Released: June 10, 1992

By the Commission: Commissioner Duggan concurring in part and dissenting in part and issuing a statement.

1. On March 27, 1991, we released a Notice of Proposed Rule Making (Notice) [FN1] seeking comments on whether we should clarify our policy governing bundling of cellular customer premises equipment (CPE) and cellular service. In particular, we sought comments on whether, or on what conditions, we should allow cellular CPE and cellular service to be offered on a bundled basis, provided that service is also offered separately at a nondiscriminatory price. Numerous parties filed comments [FN2] and reply comments [FN3] in response to our Notice. [FN4] Based on our careful analysis of all the comments and issues, [FN5] we are clarifying and modifying our policy to allow cellular CPE and cellular service to be offered on a bundled basis, provided that service is also offered separately at a nondiscriminatory basis. Our decision is based on the unique conditions in the cellular market today and on the public interest benefits associated with bundling in that market.

2. In the Second Computer Inquiry proceeding, the Commission required that common carriers sell or lease CPE separate and apart from the carrier's regulated services, and that new CPE be untariffed. [FN6] By requiring common carriers to offer unbundled CPE and transmission services, the Commission wanted to assure that customers have the ability to choose their own CPE and service packages to meet their communication needs [FN7] and that they not be forced to buy unwanted carrier-supplied CPE in order to obtain necessary transmission service. The Commission was also concerned that consumers who do not use carrier-provided CPE might find themselves subsidizing consumers who do use carrier-provided equipment, [FN8] and that independent CPE vendors might be forced to compete against below-cost, tariffed CPE because part of the CPE costs would be recovered through regulated tariffed service rates.

3. Subsequently, in authorizing commercial cellular service for the first time in 1981, the Commission stated:

> Under our Second Computer Inquiry, new terminal equipment is to be deregulated (i.e., unbundled and detariffed) after March [1], 1982. Because cellular service is a new service for which its mobile equipment has never been tariffed, we will require that it be unbundled and detariffed (untariffed) from the start. [FN9]

The Commission further indicated in Cellular CPE, 57 RR2d 989, 990 (1990), that the provision of cellular CPE should be left largely to the marketplace, on a competitive, unregulated basis.

4. On December 23, 1988, the National Cellular Resellers Association (NCRA) filed a petition for declaratory ruling requesting that the Commission institute a proceeding to declare that certain practices on the part of facilities-based cellular carriers violate the unbundling policy, citing ITT World Communications, Inc. v. TRT Telecommunications Corp., 51 RR2d 1386 (1982) (ITT World). [FN10] NCRA

alleged that the carriers' bundling practices were anticompetitive and unlawful. Cellular carriers and the cellular industry trade associations opposed NCRA's petition, asserting that the allegations of anticompetitive practices were unsubstantiated. In their view, marketing packaged deals is not prohibited bundling because CPE and service are also available separately and cellular service is priced identically to the packaged cellular service.

5. On March 27, 1991, we instituted this Rule Making proceeding to develop a complete record on the status of the bundling policy in the current cellular marketplace. As part of this proceeding, we indicated that NCRA's petition and the comments that were filed in response to NCRA's petition were to be made a part of the record. [FN11] We also indicated that this proceeding was being initiated to determine whether the cellular bundling policy should be eliminated, modified or clarified. [FN12]

6. Our Notice indicated that it was appropriate to reevaluate our bundling policy in light of changes that have occurred in the cellular industry. We indicated generally that bundling might present no problems as long as the markets for the components of the bundle are competitive. Thus, we proposed to look at the competitiveness of the cellular CPE market and the competitiveness of the cellular service market. In view of the Commission's concern that customers have the ability to choose their own CPE and service packages to meet their own communication needs and that they not be forced to buy unwanted carrier-provided CPE in order to obtain necessary service, we also asked whether consumers would be harmed by permitting bundling. In addition, we sought comment on the public interest benefits of permitting bundling. [FN13] Finally, we tentatively concluded that the current lack of regulation of the cellular industry reflects the competitiveness of the industry, and we asked for comments on the status of federal and state regulation of cellular service.

7. We have analyzed the record before us in light of the public interest objectives underlying the Commission's cellular bundling policy. This record shows that while the cellular CPE market is competitive, the cellular service is not fully competitive, thus leaving open the possibility that bundling may be used for anticompetitive purposes. Nevertheless, we do not believe that the potential for carriers to engage in anticompetitive conduct provides a basis to prohibit bundling per se. Despite some concerns raised about the status of competition in the cellular service market, the record supports the conclusion that modifying the bundling policy is in the public interest because the public interest benefits of bundling in the cellular market outweigh the potential for competitive harm. See paras. 19-21, infra. These benefits include the provision of discounted CPE to customers who otherwise would not subscribe to cellular service and the promotion of efficient spectrum utilization by adding new customers to cellular service. Accordingly, we conclude that it is in the public interest to clarify and modify our policy to allow cellular CPE and cellular service to be offered on a bundled basis, provided that the cellular service is also offered separately on a nondiscriminatory basis.

8. In our Notice, we indicated that the cellular CPE market appears to be extremely competitive both locally and nationally and that this competition has resulted in the widespread availability of cellular CPE from a multiplicity of vendors. In order to verify these assumptions, we solicited information on cellular manufacturers, including the number of national and international manufacturers and their market shares, and how cellular CPE is distributed today.

9. The record is uncontroverted that the cellular CPE market is extremely competitive, both locally and nationally, and that this competition has resulted in the widespread availability of cellular CPE. The commenters indicate that there are between 17 and 25 CPE manufacturers who distribute more than 28 brands of cellular telephones under both primary and secondary brand labels. [FN14] They note that CPE is manufactured in the United States, Canada, Japan, and Europe. The parties indicate that, because of relatively low barriers to entry, the number of CPE manufacturers continues to grow annually. The information submitted by the

commenters shows that no single manufacturer is dominant and none has a market share in excess of 20%. CTIA points out that, as a result of vibrant competition, the average price of cellular telephones has dropped from $2,500 in 1984 to $400 today. [FN15] Moreover, CPE is marketed for sale, rent or lease by facilities-based carriers as well as by agents, resellers, independent outlets, specialty shops, automotive dealers, and department stores. In view of the large number of CPE manufacturers competing in the United States cellular industry and the fact that new manufacturers are continuously entering the market, [FN16] and given the broad national distribution network for cellular CPE, it appears unlikely that one manufacturer can control the market. [FN17]

10. The Commission tentatively concluded in the Notice that the cellular service market is sufficiently competitive to prevent bundling from adversely affecting competition in the cellular CPE market. In reaching this conclusion, the Commission indicated that the cellular industry has grown considerably and that facilities-based carriers within each market compete not only against each other, both directly and through agents, but also with numerous resellers. It also indicated that the current duopoly structure of the cellular industry "provides the potential for each facilities-based carrier to possess relatively equal power in the service area and protects the public from the dangers of potential anticompetitive abuse arising from the joint provision of cellular service and CPE." [FN18] Finally, insofar as bundled offerings of cellular CPE and cellular service require that customers obtain service from a specified carrier for a fixed term, we asked whether such agreements might be discriminatory or be used to eliminate competition within the cellular market.

11. The record is not conclusive as to whether the service market is fully competitive. [FN19] In this regard, in the Cellular Report and Order, 86 FCC2d at 474-82, which established the cellular duopoly market structure, the Commission concluded that "even a marginal amount of facilities-based competition will foster public benefits of diversity of technology, service and price." Id. at 478. Although the record contains a limited amount of empirical data, it appears that facilities-based carriers are competing on the basis of market share, technology, service offerings, and service price. [FN20] However, as the FTC staff points out, the current Commission rules allowing no more than two facilities-based carriers per market place an absolute barrier to entry in the provision of wholesale cellular service. [FN21] Moreover, while resellers may help deter price discrimination, it does not appear that they compete effectively with the two facilities-based carriers in each market. In addition, while it appears that existing services, such as paging, private radio, certain landline services, and possible future services such as personal communications, Mobile Satellite Service, and specialized mobile radio services have the potential to compete with cellular, the record does not support a finding that they currently constrain facilities-based cellular carriers from acting anticompetitively. [FN22] Therefore, we agree with the DOJ that in the absence of any evidence (such as price and cost data), it is difficult to conclude that the cellular service market is fully competitive. [FN23]

12. Finally, the record reveals that an integral part of any packaged offering of cellular CPE and service is the mandatory service requirement. As we noted in the Notice, carriers can use the minimum service commitment as a vehicle for predatory pricing or other anticompetitive conduct only if they can eliminate competition and monopolize the cellular market. See Matsushita Electrical Industrial Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986). There is no evidence that this has occurred or is even possible, particularly because the minimum service periods of three months to one year, identified by evidence in the record, are relatively short. Cf. Comsat, 5 FCCRcd 4869 (1990), and RCA Satcom, 84 FCC2d 353 (1980). (These cases involve regulated domestic satellite services and articulate the Commission's recognition of the benefits that such contracts bring to the carrier-customer relationship).

13. Even if we were to assume that a facilities-based carrier has the potential to act anticompetitively in its Cellular Geographic Service Area (CGSA), based on the current structural conditions in the cellular service and CPE markets, it appears

unlikely that any carrier engaged in bundling would be able to restrict competition in the CPE market. Specifically, the conditions necessary to obtain an anticompetitive outcome do not appear to exist in the cellular industry. First, it does not seem likely that individual cellular companies which operate in local markets possess market power that could impact the numerous CPE manufacturers operating on a national and international basis. According to CTIA, there are 125 facilities-based cellular system operators in this country and more than 6,000 cellular agents. [FN24] We agree with the FTC Staff that under these conditions, a CPE manufacturer foreclosed by one cellular service company from its CGSA easily could sell its equipment to other cellular carriers operating in many other CGSAs. Furthermore, we agree with the DOJ that cellular carriers do not have the potential to engage in sustained predatory pricing practices in the CPE retail market. As the DOJ points out, even if the two facilities-based carriers in a market cornered the local retail CPE market and began charging high CPE prices, other CPE providers from outside of the local market could supply retailers with affordable CPE, thus undercutting a carrier's high-priced CPE. [FN25] Customers, of course, would be able to purchase the lower-priced CPE and obtain cellular service at the same rates as if the customer had bought the CPE from the carrier because cellular service will remain available on an unbundled, nondiscriminatory basis. Under these circumstances, it is unlikely that carriers engaged in bundling could charge supracompetitive prices and still deter retailers from carrying CPE. Thus, we agree with the FTC Staff's conclusion that "[i]f individual cellular service companies do not possess market power in the sale of cellular service on a national level, it is unlikely that foreclosure of the CPE market can be successful." [FN26] The possibility that one carrier could dominate the CPE market is further diminished by the fact that most carriers do not manufacture CPE and because most cellular service markets are duopolistic rather than monopolistic, a carrier's market power is attenuated.

14. It is also uncontested that there is a robust level of competition that exists in the CPE markets notwithstanding the common marketing practice of packaging CPE and cellular service. This marketing practice of packaging CPE and cellular service has existed for several years and has benefited consumers. Accordingly, we believe that the information submitted in this proceeding reveals that if the Commission clarified its policy to permit bundling, facilities-based carriers engaged in bundling would not be able to adversely affect competition in the cellular CPE market.

15. Finally, two parties allege that facilities-based carriers have entered into exclusive dealing agreements with CPE providers. [FN27] However, the details of these agreements are not revealed. Therefore, the impact of such arrangements cannot be thoroughly evaluated. Nevertheless, there is no evidence that cellular carriers refuse to provide service to customers that purchase another brand of CPE. Furthermore, although there are general allegations that these exclusive dealing arrangements preclude agents from offering other brands of CPE to customers, no specific evidence has been raised to support these allegations.

16. ICDMA contends that carriers' exclusive dealing arrangements with CPE manufacturers, coupled with their ability to engage in price packaging, creates the potential for anticompetitive abuse. It therefore proposes several safeguards to reduce this potential. First, it states that if a carrier is the exclusive distributor of a particular manufacturer's CPE, the carrier should not be allowed to create price packaging that includes the cellular CPE unless the carrier makes that CPE available to independent retailers in its service area. Second, it provides that carriers should not be allowed to offer price reductions for CPE included in carriers' price packages offered at the retail level (when compared to the stand-alone CPE retail prices offered by the carrier) that are greater than the highest level of activation commissions paid to independent retailers. Third, it asserts that activation term commitments for subscribers purchasing carrier provided retail price packages should be for the same period of time as the term commitments made by subscribers purchasing their service through independent retailers, which thereby earn activation commissions for those retailers.

17. We find that ICDMA's safeguards are not warranted because there is no evidence in the record before us revealing that the anticompetitive abuses which ICDMA is addressing are presently occuring. If such evidence were presented, however, we would consider adopting safeguards similar to those proposed by ICDMA. The record is also void of any evidence showing that these existing exclusive dealing arrangements will potentially have an anticompetitive impact on competition in the CPE market. [FN28] Accordingly, we do not here adopt ICDMA's safeguard proposals.

18. Furthermore, the record does not demonstrate a reason to be concerned about future exclusive dealing arrangements. First, it appears that carriers are primarily motivated to sell more service and are not particularly interested in entering into such agreements with CPE providers because, as Century has pointed out, their customers demand that they carry the widest variety of CPE possible. [FN29] Second, if one carrier managed to eliminate all agents and only offered a bundle of service and one CPE manufacturer's CPE, a customer could always go elsewhere or to another carrier to get CPE. Third, current nondiscrimination requirements preclude a cellular carrier from refusing to provide service to a customer on the basis of what CPE the customer owns. [FN30] Fourth, because cellular service is offered in local markets, exclusive dealing arrangements would not eliminate international and national CPE providers in the absence of a nationwide conspiracy by cellular carriers to eliminate CPE manufacturers. Therefore, it is highly unlikely, even theoretically, that a future exclusive dealing arrangement could be successful in eliminating a CPE manufacturer. Nevertheless, if in the future, it comes to our attention that carriers' exclusive distribution agreements with CPE manufacturers are resulting in anticompetitive abuse, we will not hesitate to revisit this area.

19. Notwithstanding the state of competition in the cellular service industry, there appear to be significant public interest benefits associated with the bundling of cellular CPE and service. [FN31] In this regard, the record supports a finding that the high price of CPE represents the greatest barrier to inducing subscription to cellular service. [FN32] Thus, as several of the commenters, including the DOJ, have pointed out, bundling is an efficient promotional device which reduces barriers to new customers and which can provide new customers with CPE and cellular service more economically than if it were prohibited. [FN33] Moreover, packaging cellular CPE and service is a common and generally accepted practice in the cellular industry. Finally, the FTC Staff explains that a decision to prohibit introductory discounts "may cause the companies to replace these discounts with promotional expenditures that are more costly and less likely to be directly appropriated by the customer." [FN34]

20. Moreover, with the influx of new subscribers due to the bundling of cellular CPE and service, the fixed costs of providing cellular service are spread over a larger population of users, achieving economies of scale and lowering the cost of providing service to each subscriber. [FN35] Rapid growth of the subscriber base also promotes the efficient use of the spectrum. In addition, clarifying our policy to allow the bundling of cellular CPE and cellular service furthers the Commission's goal of universal availability and affordability of cellular service and thus promotes the continued growth of the cellular industry. [FN36] We also find that bundling can assist in the conversion to digital. As the DOJ and the FTC Staff point out, initially, digital deployment will require the use of dual-mode telephones, which will, most likely, be slightly larger, heavier and more expensive than analog models. A prime means of marketing these phones will be through attractively priced packages of service and new equipment.

21. Finally, bundling may be used by carriers as an efficient distribution mechanism. Here, the FTC Staff point out that because a decision as to how to distribute one's product may have a significant impact on the type of service or the quality of the product provided, "interference in these relationships should be approached with caution." [FN37]

22. The Commission tentatively concluded in the Notice that consumers are not likely to be harmed by permitting bundling. The Commission stated that modifying

the bundling policy probably will not affect cellular service prices. The Commission also indicated that discounted CPE appears to be the result of agents using their commissions to offset or hold down the price of CPE. If CPE discounts are eliminated, it continued, carriers probably will continue to pay their agents commissions because such payments are market driven, and it is unlikely that the cellular service prices would decrease. Because it appears that agents are using their carrier-paid commissions to hold down the prices they charge their customers, the Notice requested comments on whether this is the type of cross-subsidy that public policy should prevent and whether a modification of the bundling policy would adversely affect cellular service prices.

23. Based on the record before us, it appears that subscribers may be benefiting from the current cellular industry practice of bundling cellular CPE and cellular service. As a result of the lower prices for cellular CPE, [FN38] individuals who would otherwise decline cellular service are becoming subscribers, thereby spreading the cost of providing cellular service. Moreover, there is no evidence that bundling cellular CPE and service has led to an increase in service prices. [FN39] Nor has evidence been submitted to support the claim that bundling leads to discriminatory cellular service rates. The industry practice is that cellular service is offered separately from CPE on a nondiscriminatory basis.

24. The record is also inconclusive as to whether carriers are using their service revenues to subsidize their bundling practices. As we pointed out in the Notice, discounted CPE appears to be the result of agents using their commissions to offset the original cost of CPE. Thus, even if cellular CPE discounts were eliminated, there is no indication that carriers would not continue to pay their agents commissions because these commissions appear to be market driven. Nevertheless, as the DOJ and the FTC Staff agreed, it is unlikely that any profit maximizing firm would set its service rates based on the size of the commissions paid to agents. [FN40] Moreover, there is no convincing evidence that if these packaging practices were eliminated, cellular service prices would decline. In any event, the potential anticompetitive impact from this type of bundling is outweighed by the public interest benefits associated with the bundling of cellular service and CPE. Finally, we agree with the DOJ that even if the elimination of bundling led to a reduction in the commissions carriers paid their agents, there would likely be a negligible effect on the marginal cost of cellular service and, therefore, no discernible impact on service rates.

25. In the Notice we tentatively concluded that the lack of state regulation of the cellular industry reflects the competitiveness of the industry and a decreasing concern that carriers are using largely untariffed cellular service to act anticompetitively in the unregulated CPE market, i.e., by raising cellular service prices to subsidize low cost CPE. The record reveals that cellular service is unregulated at the federal level and largely unregulated at the state level. [FN41] Moreover, it appears that most of those states that do regulate cellular service do not exercise rate-of-return regulation. While the non-regulation of cellular service does not in itself demonstrate that the cellular service market is competitive, it does suggest that state PUCs have chosen not to regulate cellular service because they do not consider it a monopoly service. In addition, the lack of regulation based on rate-of-return principles, combined with the absence of monopoly status for cellular carriers, significantly reduces one important motive for carriers to bundle--to build unregulated CPE costs into the service rate base and cross-subsidize at the expense of the subscriber. As the DOJ notes, "absent a guaranteed return on their cellular service investments, carriers cannot expect to recover CPE discounts by including it [the amount of the CPE discounts] in their rate base." [FN42] We agree with this conclusion.

26. In our Notice, we requested comments on the extent to which the elimination or substantial modification of the cellular CPE bundling policy would affect resellers, and the extent to which this impact should be taken into account in formulating our bundling policy.

27. The record is inconclusive as to what extent resellers would be affected if

facilities-based carriers were allowed to bundle cellular CPE and cellular service. On the one hand, many of the parties argue that resellers have not submitted specific evidence demonstrating that the current carrier practice of packaging cellular CPE and cellular service has had an adverse impact on resellers. On the other hand, other commenters, such as NCRA and NACA, argue that the anticompetitive effects of bundling are driving resellers out of business because they are unable to compete for new cellular subscribers. They argue that, unlike facilities-based carriers, resellers do not have service revenues that subsidize bundling practices. NCRA also claims that the number of resellers in existence today that are not affiliated with a facilities-based carrier is small and is declining. [FN43]

28. As the FTC Staff points out, in a case such as this where resellers are alleging that carriers are engaging in predatory pricing practices, (i.e., offering wholesale cellular service to resellers at an inflated non-cost based price and at the same time reducing the retail price charged by their retail arms through commissions or other incentive payments), it is difficult to differentiate between such predatory practices and intense retail competition that includes the use of an efficient distribution system. [FN44] We agree with the FTC Staff and the DOJ that the most efficient government policy is to allow firms the ability to choose how to distribute their own products. [FN45] Thus, to the extent that elimination of the bundling prohibition allows facilities-based carriers to utilize their preferred distribution systems more intensively, and to the extent that resellers are not part of the facilities-based cellular carriers' preferred retail distribution systems, resellers may not benefit from the elimination of the bundling prohibition. [FN46] Nevertheless, the possibility that one type of retailer may be harmed "does not provide a basis for a rule that limits the use of a potentially efficient contract or retail distribution system." [FN47] This is especially the case here where the resellers primary concern appears to stem from the rate structure that they are held to by the carriers and not the carriers' practices of offering cellular CPE and service on a bundled basis. [FN48] Moreover, the DOJ further explains that since resellers will remain able to obtain CPE to offer their customers together with service, the sole effect of allowing carriers to bundle will be to put the resellers in the same position that any distributor faces when its supplier engages in dual distribution. [FN49] We agree with the DOJ that "[s]uch dual distribution does not, in itself, raise anticompetitive effects." Finally, we note that the record shows that resellers also offer promotional packages of cellular CPE and transmission service. [FN50]

29. As we noted in the Notice, packaged offerings are commonplace in a variety of industries in which customers can purchase an array of products in a package at a lower price than the individual products could be purchased separately. [FN51] However, the Commission's prohibition of bundled offerings in the Second Computer Inquiry was based on the concern that subscribers have the ability to choose their own CPE and service packages and that they not be forced to buy unwanted carrier-supplied CPE in order to obtain transmission service. Based on our analysis of the cellular industry, we have found that while the cellular CPE industry is competitive, we are unable to conclude that the cellular service market is fully competitive.

30. Nevertheless, we do not believe that the potential for cellular carriers to engage in anticompetitive conduct provides a strong reason to prohibit bundling per se. Despite our concerns about the status of competition in the cellular service market, the records supports the conclusion that clarifying the current bundling policy to allow facilities-based carriers to bundle cellular CPE and service would not have an adverse impact on the cellular CPE market. Moreover, the theoretical potential for this or other anticompetitive behavior is outweighed by the public interest benefits of permitting bundling. These benefits allow customers to obtain a wide assortment of combined CPE and service from numerous sources, including the carriers and their agents. Accordingly, we will adopt our initial proposal and allow cellular CPE and cellular service to be offered on a bundled basis, provided that the service is also offered separately at a nondiscriminatory price. [FN52] This policy will ensure that facilities-based carriers who provide cellular CPE and cellular service on a packaged basis will continue to be required to offer cellular

service to agents, resellers and other customers at a nondiscriminatory rate. [FN53] We wish to emphasize that our responsibility is to assure that the public interest, including maintaining a level playing field and fostering competition, maximizes benefits to subscribers. [FN54]

31. While we recognize the customer benefits of CPE discounting as a part of the sale of cellular service, we intend to monitor the bundling of cellular service and cellular CPE. Our continuing interest is based on our intention that bundling not be used anticompetitively. If parties can demonstrate that carriers' incentive offerings lead to anticompetitive abuses, the Commission will be open to further action.

32. Finally, the parties generally agree with our position in the Notice that there is no reason to institute a federal bundling policy that preempts state action in this area. Accordingly, while we modify our current cellular bundling policy, we will not preempt state regulatory action even if it is more restrictive.

33. Authority for the changes to the bundling policy adopted herein is contained in Sections 1, 4(i), 4(j) and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. Sections 151, 154(i), 154(j) and 303(r).

34. Accordingly, IT IS ORDERED that the Commission's cellular bundling policy is clarified and modified as set forth above.

35. IT IS FURTHER ORDERED that the changes made herein WILL BECOME EFFECTIVE (30) days after publication in the Federal Register.

36. IT IS FURTHER ORDERED that this proceeding is HEREBY TERMINATED.

Donna R. Searcy

Secretary

FN1. Bundling of Cellular Customer Premises Equipment and Cellular Service, 6 FCCRcd 1732 (1991), appeal dismissed, National Cellular Resellers Association v. FCC, No. 91-1269 (D.C.Cir. April 2, 1992).

FN2. See Appendix A for list of commenters. Late-filed pleadings were filed by David A. Wolber, Don Philpott, John Webb and David M. Block. We will accept these comments in the interest of obtaining a complete record upon which to base our decisions in this proceeding. On May 10, 1991, the National Association of Cellular Agents (NACA) requested a 90 day extension of time to file comments. By Order, Mimeo No. 13260 (May 28, 1991), the Common Carrier Bureau denied the request, finding that NACA had failed to show good cause for the requested 90 day extension of time.

FN3. Reply comments were originally scheduled to be filed on June 4, 1991. On May 28, 1991, in response to a request from Telocator, the deadline for filing reply comments was extended to June 19, 1991. See Order, 6 FCCRcd 3374 (1991).

FN4. Ex parte comments were filed by several parties and, in accordance with Section 1.1206 of our rules, have been made part of the record in this proceeding.

FN5. We have analyzed all of the arguments contained in the comments before resolving this rulemaking proceeding. However, not all of the points raised in the comments are discussed in the Report and Order for reasons of brevity.

FN6. Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), Final Decision, 77 FCC2d 384; modified on recon., 84 FCC2d 50 (1980); further modified 88 FCC2d 512 (1981), aff'd sub nom., Computer and Communications Industry Ass'n v. FCC, 693 F.2d 198 (D.C.Cir.1982), cert. denied, 461 U.S. 938 (1983), aff'd on second further recon., FCC 84-190, (released May 4, 1984).

FN7. Id. at 443-43, para. 149.

FN8. Id. at 444-45, para. 154.

FN9. Cellular Communications Systems (Cellular Report and Order), 86 FCC2d 469, 497 (1981) modified, 89 FCC2d (Reconsideration Order), further modified, 90 FCC2d 571 (1982) (Further Reconsideration Order) appeal dismissed sub nom. U.S. v. FCC, No. 82-1526 (D.C.Cir. March 3, 1983).

FN10. NCRA indicated in its petition that it had filed pleadings in another proceeding concerning the Commission's cellular resale policies and that those pleadings referenced the Commission's unbundling policy. See Petitions for Rule Making Concerning Proposed Changes to the Commission's Cellular Resale Policies, 6 FCCRcd 1719 (1991). NCRA requested that the pleading filed in the resale proceeding be incorporated in its petition dealing with bundling.

FN11. Accordingly, we declined NCRA's request to act formally on its petition for declaratory ruling at that time.

FN12. On June 3, 1991, NCRA filed a petition for review in the United States Court of Appeals for the District of Columbia Circuit of the Commission's decision in Bundling of Cellular Customer Premises Equipment and Cellular Service. National Cellular Resellers Association v. FCC, D.C.Circuit No. 91- 1269. That proceeding was dismissed on April 2, 1992. See note 1, supra.

FN13. We also requested comment on the relative importance of the factors incorporated into our analysis and on any other factors that we did not address. CTIA asserts that in analyzing the effects of packaging on consumer welfare, the Commission should utilize the Sherman Act antitrust standard applied in Jefferson Parish Hospital District No. 2 v. Hyde, 466 U.S. 2 (1984). Under that standard, tying arrangements are per se illegal. CTIA argues that illegal tying arrangements do not exist in the cellular industry because consumers are not being forced to purchase CPE. We decline to adopt CTIA's narrow standard which focuses exclusively on anticompetitive effects because, as the Commission has noted in the past, the public interest standard encompasses matters that go beyond the promotion of competition. Cellular Report and Order, 86 FCC2d at 486.

FN14. See, e.g., Herschel Shosteck Associates, Ltd., Advance Data Flash Cellular Brand Sales, Vol. 6, No. 2, Quarterly Survey (September 1991).

FN15. CTIA Comments at 13.

FN16. See e.g., Rhonda L. Wickham, Plenty of Portables, Cellular Business, Vol. 8, June 1991.

FN17. For its part, the North American Telecommunications Association (NATA) argues that a finding now that the CPE market is competitive does not justify a reversal of the unbundling requirement, because the Commission in the Cellular Report and Order relied on the existence of CPE competition when it mandated the unbundling of cellular CPE. NATA Comments at 12. We agree with NATA that it would be insufficient to permit bundling based solely on a finding that the CPE market is competitive. Nevertheless, the competitiveness of the CPE market is an important factor for purposes of determining whether to modify the cellular bundling policy. The Commission in the Second Computer Inquiry stated that:

> If the markets for the components of the commodity bundle are workably competitive, bundling may present no major societal problems as long as the consumer is not deceived concerning the content of the bundle.

Second Computer Inquiry, 77 FCC2d at 443 n. 52. Moreover, as discussed below, in addition to considering any concerns that flow from the status of competition in the relevant markets, we have also examined the public interest benefits of permitting bundling.

FN18. Notice at para. 13.

FN19. NCRA argues that, in analyzing whether the cellular market is fully competitive, the Commission in the Notice should have utilized the same standards used to evaluate market conditions in the interexchange markets, citing Interexchange Market Regulation Order, 5 FCCRcd 2627, 2639-40 (1990). It asserts that the application of different standards is arbitrary and capricious unless the Commission can offer a reasonable explanation. As discussed below, our decision in this proceeding is not dependent on a conclusion that cellular service markets are fully competitive. Accordingly, we need not address NCRA's concerns regarding the market analysis suggested in the Notice.

FN20. Several parties argue that in some markets, the cellular service prices are similar, but there is no indication that anticompetitive conduct is occurring. As we stated in the Cellular Resale Notice of Proposed Rule Making and Order, 6 FCCRcd 1719 (1991), "similarity in price without more may equally indicate vigorous price competition between facilities-based carriers in the same market." Id. at 1725, citing Turner, The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusal to Deal, 75 Harv.L.Rev. 655 663-73 (1962).

FN21. According to the FTC Staff, the Herfindahl-Hirschman Index, which is used to measure the extent of market concentration, indicates that the cellular service market would be 5000, well above the highly concentrated threshold contained in the Department of Justice Merger Guidelines. FTC Staff Comments at 11-12.

FN22. NCRA and Tandy point out that the Commission in Competitive Carrier Rule Making, 98 FCC2d 1191, 1204 n. 41 (1984), classified facilities-based carriers as "dominant carriers," a classification which suggests that both carriers in each market jointly possess market power and are capable of engaging in anticompetitive conduct. NCRA asserts that the Commission has not reclassified facilities-based carriers as non-dominant and that eliminating or modifying the bundling policy requires a demonstration that cellular service carriers do not exercise market power. Therefore, it asserts that the Commission's tentative conclusion that the cellular service market is sufficiently competitive so that bundling would not affect competition in the cellular CPE market is unsupported. NCRA Comments at 9 n. 9. We do not agree that the Competitive Common Carrier Rule Making requires that carriers must be found non-dominant before the bundling policy is modified. The Commission's classification of carriers as dominant or nondominant in the

Competitive Common Carrier Rule Making does not, without further analysis, determine whether carriers should be allowed to bundle cellular CPE and transmission services. We must take into account other factors, including the impact on competition in the cellular CPE market and the public interest benefits of bundling. To the extent that NCRA and Tandy challenge the Commission's conclusion that bundling would not affect competition in the cellular CPE market, see discussion in paras. 13-18, infra.

FN23. The DOJ Comments at 5.

FN24. CTIA Comments at 14.

FN25. The DOJ Comments at 8-9.

FN26. FTC Staff Comments at 23.

FN27. Cellnet, a reseller in the Detroit area, maintains that it has been foreclosed from marketing certain brands of CPE by virtue of exclusive arrangements between particular manufacturers and one of the facilities-based carriers in the Detroit market. Cellnet Comments at 11. In addition, Cellular Marketing, Inc., an independent agent and reseller in the Houston area, also contends that such exclusive arrangements between one of the facilities-based carriers in the Houston area and certain cellular CPE suppliers have prevented its agents from buying CPE at the lowest cost. Cellular Marketing Comments at 5. No more specific details are provided.

FN28. We indicated in the Notice that exclusionary conduct reducing the likelihood of price decreases should be considered a form of monopoly or market power because such conduct can delay or prevent prices from falling by preventing the entry of or raising the costs of more efficient competitors. See Krattenmaker, Lande, and Salop, Monopoly Power and Market Power in Antitrust Law, 76 Georgetown L.J. 241, 259 (1987). In this regard, there is no evidence in the record to show that, in those instances where cellular carriers have entered into exclusive distribution agreements with CPE manufacturers, CPE prices have increased or that CPE competition has diminished.

FN29. Century Comments at 4.

FN30. Several parties, such as NCRA, NACA and Tandy, argue that, in the long run, allowing duopolists with market power to bundle cellular CPE and service drives out independent CPE competition, reduces the number of CPE/service choices to two, and eventually leads to higher service prices. This worst case scenario is unlikely to occur for the reasons stated above. For there to be only two CPE offerings nationwide would require a conspiracy of cellular carriers to eliminate CPE manufacturers. Such anticompetitive conduct could be prevented through application of the state and federal antitrust laws.

FN31. As we pointed out in the Notice, packaged offerings are commonplace in a variety of industries in which customers can purchase a number of goods in a package at a lower price than the individual goods could be purchased separately. Moreover, under the federal antitrust laws, packaged offerings are legal unless they constitute an illegal tie-in or represent an unlawful exercise of monopoly power.

See Jefferson Parish Hospital District No. 2 v. Hyde, 466 U.S. 2 (1984); United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 391 (195); and Hunt-Wesson Foods, Inc., v. Ragu Foods, Inc., 627 F.2d 919, 924 (9th Cir.1980).

FN32. The majority of the commenters believe that the increasing rate of cellular subscribership in the United States is, in large part, due to the sharp price reductions of cellular telephones. See e.g., CTIA Comments at 5- 6; Cellular Communications Comments at 13; and New Vector Reply Comments at 2.

FN33. NCRA maintains that unless evidence has been submitted showing that the joint provisioning of cellular service and CPE yields some production efficiency, the cost of bundled service and CPE can never be appreciably lower than the sum of the cost of each component. NCRA Comments at 17. However, as the FTC Staff has pointed out, packaged offerings can be used to reduce transaction and information costs as well as to lower the cost of distributing the products. FTC Staff at 16-17.

FN34. FTC Staff Comments at 17-18.

FN35. CTIA points out that in January 1985, the capital investment per subscriber was $3872.93; in January 1988, it was $1951.11; and in January 1991, it was $1189.01. CTIA Comments at 19.

FN36. Centel Comments at 3-4.

FN37. FTC Staff Comments at 14.

FN38. For example, Century notes that in 1988, the average price of a cellular telephone was $1,000, while in 1990 the average price was $400. Century Comments at 2.

FN39. According to NCRA, cellular is a declining-cost industry; each carrier's ratio of fixed-to-total costs is very high; original plant has been substantially depreciated; and consumer demand grows at tremendous rates each year. NCRA contends that under these conditions, rates should be falling. NCRA Comments at 10-11. However, McCaw cites industry studies showing that from 1987 to 1991, cellular service prices declined in absolute terms in one third of the top 30 markets and in additional markets when adjustments for inflation are considered. McCaw Reply Comments at 9.

FN40. In this regard, NCRA and Tandy argue that bundling causes existing cellular subscribers to subsidize CPE purchases from new users. NCRA Comments at 18-19; Tandy Comments at 19-20. We reject this argument. As DOJ has observed, this argument presumes that carriers set their rates on the basis of their average costs. However, in the short run, profit-maximizing carriers will set their rates based on variable costs, i.e. the costs they can control by increasing or decreasing output. DOJ states that demand requires a carrier to try to maximize the difference between revenue and total variable cost. Once the carrier has signed up a new customer, the commission it paid its agent is a sunk cost that has no unique impact on the variable cost of providing cellular service. Thus, the service rate charged would not vary with the size of commissions paid to agents. DOJ Comments at 10-11. In short, the CPE expenses are treated as any other cost of securing a subscriber, e.g., advertising.

FN41. CTIA submits data showing that 12 states fully regulate cellular service, 12 are partially regulated and the remaining states impose no regulations. According to CTIA, a state which regulates cellular service requires a Certificate of Public Convenience and Necessity (CPCN) and tariffs, for both wholesale and retail offerings. A state which partially regulates typically requires a CPCN and tariffs at the wholesale level but not at the retail (subscriber) level. A state that is not regulated does not require cellular carriers to obtain CPCN's or file tariffs. CTIA Comments at Attachment D.

FN42. The DOJ Comments at 29.

FN43. NCRA Comments at 14.

FN44. FTC Comments at 13-14.

FN45. Id. at 15.

FN46. See FTC Staff Comments at 15.

FN47. Id. at 15.

FN48. Any restrictions on resellers' ability to buy packages of CPE and service on the same basis as other customer would be unlawful. See Petitions for Rule Making Concerning Proposed Changes to the Commission's Resale Policies, (Cellular Resale NPRM/Order), 6 FCCRcd 1719 (1991). Resellers also appear to be concerned that service prices may be subsidizing CPE prices in packaged offerings. NCRA Comments at 3. In this regard, see para. 24, supra and note 53, infra.

FN49. The DOJ Comments at 12.

FN50. NYNEX states that resellers have offered promotional packages where the facilities-based carriers or its retail affiliate do not offer such packages. NYNEX Comments at 10. See also Southwestern Bell Comments at 14.

FN51. See Notice, 6 FCCRcd at 1737, n. 21.

FN52. In addition, we note that cellular carriers will still have to comply with all applicable state and federal antitrust laws. See, e.g., Section 3 of the Clayton Act, 15 U.S.C. Section 14.

FN53. In its petition for declaratory ruling filed on December 23, 1988, NCRA contended that carriers' bundling or packaging practices are inconsistent with our decision in AT & T Opportunity Calling, ENF-84-36, E-84-28 (released April 4, 1985) (Opportunity Calling). NCRA maintained that carriers' offerings patently discriminate in favor of new customers who receive a discount or rebate and against customers who do not receive such a discount or rebate. We disagree with NCRA that the Common Carrier Bureau's (Bureau) decision in Opportunity Calling provides a

basis for finding that cellular carriers' bundling or packaging practices are impermissible. In Opportunity Calling the Bureau indicated (in dictum) that circumstances could arise in which rate preferences for new customers might be unlawful. As indicated earlier, however, cellular service is not subject to cost based rate-of-return regulation and there is no conclusive evidence here that cellular carriers use their cellular service revenues to subsidize their bundling practices. Hence, the record does not support a finding that new cellular customers are receiving rate preferences for cellular service through cross-subsidization. Moreover, as discussed in paras. 19-21, supra, bundling is an efficient promotional device which appears to create benefits for all cellular customers.

FN54. In view of our determination that such bundling activities are not precluded under our new policy, we reaffirm our dismissal of NCRA's petition for declaratory ruling filed on December 23, 1988. As noted above, the record before us does not support NCRA's petition.

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